

AASB Basis for Conclusions

This AASB Basis for Conclusions accompanies, but is not part of, AASB 17.

Introduction

AusBC1 This Basis for Conclusions summarises the Australian Accounting Standards Board's (AASB) considerations in reaching the conclusions regarding the substantive Australian-specific issues pertinent to IFRS 17 *Insurance Contracts* as incorporated into AASB 17 *Insurance Contracts*. In making decisions, individual Board members gave greater weight to some factors than to others.

Australian-specific issues

AusBC2 In issuing IFRS 17 the International Accounting Standards Board (IASB) replaced its existing Standard on insurance, namely IFRS 4 *Insurance Contracts*. IFRS 4 allowed entities to use a wide variety of accounting practices for insurance contracts, reflecting national accounting requirements. In the Australian context, those national accounting requirements (including Reduced Disclosure Requirements (RDR) concessions) were contained in:

- (a) AASB 4 *Insurance Contracts*;
- (b) AASB 1023 *General Insurance Contracts*;
- (c) AASB 1038 *Life Insurance Contracts*; and
- (d) Interpretation 1047 *Professional Indemnity Claims Liabilities in Medical Defence Organisations*.

AusBC3 In addition, AASB 1056 *Superannuation Entities* includes requirements applicable to a superannuation entity acting in the capacity of an insurer.

AusBC4 IFRS 17 was developed by the IASB from a for-profit perspective. Accordingly, and consistent with the AASB's *Process for Modifying IFRSs for PBE/NFP*, the AASB considered whether it would be suitable for not-for-profit (NFP) entities.

AusBC5 Within the context of replacing existing Australian requirements and addressing NFP issues, Australian-specific issues that are the subject of this Basis for Conclusions relate to the implications for:

- (a) AASB 4, AASB 1023 and AASB 1038 (including Australian-specific disclosure requirements) – see paragraphs AusBC6–AusBC11;
- (b) Interpretation 1047 – see paragraphs AusBC14–AusBC17;
- (c) AASB 1056 – see paragraphs AusBC18–AusBC22;
- (d) NFP and public sector entities (including for-profit public sector entities) – see paragraphs AusBC23–AusBC30; and
- (e) RDR – see paragraphs AusBC31–AusBC32.

Some of these issues have been resolved through the issue of AASB 17, others will be the subject of further due process (including in a forthcoming ED on Australian-specific issues arising from AASB 17), as noted where relevant below.

Implications for AASB 4, AASB 1023 and AASB 1038

AusBC6 The AASB noted that adopting IFRS 17 would supersede AASB 4, AASB 1023 and AASB 1038 and therefore change current accounting requirements for insurance contracts. The AASB acknowledged that doing so would improve financial reporting in some respects but not in other respects.

AusBC7 Regarding the key aspects, the AASB noted that:

- (a) the main improvements include:
 - (i) greater clarity around the accounting for acquisition costs, particularly for general insurance; and

- (ii) greater alignment with other industries of the basis for revenue recognition for insurance contracts with coverage periods greater than one year; and
 - (b) the main areas not improved include:
 - (i) use of historical (inception-date) discount rates in accounting for the contractual service margin (CSM) under the 'general model';
 - (ii) use of 'coverage period' (rather than pattern of service provision) as the basis for recognising the CSM in profit over the contract life; and
 - (iii) the level of aggregation of contracts for accounting purposes.
- AusBC8 In weighing up these issues, the AASB also acknowledged the precedent it established when it decided not to adopt IAS 26 *Accounting and Reporting by Retirement Benefit Plans* in favour of retaining the Australian accounting requirements specified in AAS 25 *Financial Reporting by Superannuation Plans*. This decision was subsequently reconfirmed when the AASB issued AASB 1056 to supersede AAS 25.
- AusBC9 In considering the facts and circumstances surrounding the AASB's decisions not to adopt IAS 26 (and thereby have an exception to its IFRS adoption policy), the AASB concluded that the legislative environment as well as tailored financial reporting requirements for superannuation entities (which were not adequately addressed in IAS 26) justified the need for a specific Australian pronouncement (see paragraphs BC7–BC11 of AASB 1056). In contrast, overall, the AASB concluded that IFRS 17 represents a comprehensive, internationally consistent, set of financial reporting requirements for Australian insurers, despite the issues noted in paragraph AusBC7(b).
- AusBC10 On balance, the AASB considered that the benefits arising from international harmonisation in relation to the accounting for insurance contracts, and the greater alignment of the basis for revenue recognition with other industries noted in paragraph AusBC7(a)(ii), outweighed the drawbacks noted in paragraph AusBC7(b). Accordingly, the AASB decided to supersede AASB 4, AASB 1023 and AASB 1038 (and Interpretation 1047 – see paragraphs AusBC14–AusBC17) for for-profit private sector entities with the issue of AASB 17. NFP private sector entities and public sector entities are discussed in paragraphs AusBC23–AusBC30.
- AusBC11 The AASB noted that a consequence of its decision to supersede AASB 1023 and AASB 1038 is that Australian specific disclosures (eg paragraphs 17.8 and 17.10(c) of AASB 1038 relating to regulatory capital disclosures and conformance with the *Life Insurance Act 1995*) are no longer required. However, as a separate project the AASB intends to review the usefulness and necessity of those disclosures under AASB 17 at a future date prior to AASB 17 becoming mandatory.
- AusBC12 The AASB further considered the interaction between AASB 4, AASB 1023 and AASB 1038, noting that compliance with either AASB 1023 or AASB 1038 simultaneously achieved compliance with AASB 4. However, the AASB observed that this fact was not explicitly stated in AASB 4 itself, which resulted in divergent interpretations of whether an insurer could apply either of the AASB 9 *Financial Instruments* deferral or overlay approaches introduced with AASB 2016-6 *Amendments to Australian Accounting Standards – Applying AASB 9 Financial Instruments with AASB 4 Insurance Contracts*.
- AusBC13 The AASB decided to clarify paragraph Aus3.1 and insert paragraph Aus3.2 in AASB 4 to replicate similar wording already present in AASB 1023 and AASB 1038 to highlight the simultaneous compliance noted above. Furthermore, the AASB decided to clearly indicate that liabilities in scope of AASB 1023 and AASB 1038 are included in an insurer's consideration of whether it qualifies for either the deferral or overlay approaches. The AASB noted that these amendments are purely mechanical and for clarification only, expecting no change in practice arising from these amendments.

Implications for Interpretation 1047

- AusBC14 Interpretation 1047 was originally issued in June 2002 to address divergent views as to whether a Medical Defence Organisation (MDO) should recognise a liability for future claims arising from the medical indemnity insurance it offered given the MDO had discretion on whether to pay claims made by members. The Interpretation required that a MDO recognise its obligations in a manner consistent with the principles in AASB 1023.
- AusBC15 After 1 July 2003, the *Medical Indemnity Act 2002* came into effect and regulatory arrangements allowed only authorised general insurers to offer medical indemnity insurance. In August 2016 the AASB noted feedback from staff outreach to industry stakeholders indicating that all medical indemnity insurance had, as of then, been transferred to authorised general insurers (or subsidiaries thereof).
- AusBC16 Also at its August 2016 meeting, the AASB noted that some business written by MDOs prior to 1 July 2003 could still be in existence, and therefore might still require the guidance of Interpretation 1047.

However, on balance, based on the feedback from staff outreach to industry stakeholders, the AASB concluded that any such remaining business would be immaterial to the financial statements of the affected insurers.

- AusBC17 Accordingly, the AASB decided to supersede Interpretation 1047 for for-profit private sector entities upon the adoption of IFRS 17 given it was no longer materially relevant, could result in a perceived ‘difference’ from IFRS if retained and no longer reflected predominant current practice. NFP private sector entities and public sector entities are discussed in paragraphs AusBC23–AusBC30.

Implications for AASB 1056 *Superannuation Entities*

- AusBC18 The AASB issued Exposure Draft ED 223 *Superannuation Entities* (December 2011) proposing new accounting requirements for superannuation entities as part of the AASB’s comprehensive review of AAS 25. ED 223 proposed that superannuation entities must measure any liabilities arising from insurance arrangements provided to members in accordance with the approach in AASB 119 *Employee Benefits* for defined benefit plans.
- AusBC19 The AASB issued AASB 1056 in June 2014 instead requiring that superannuation entities apply the defined benefit member liability measurement requirements of AASB 1056, as opposed to AASB 119, in response to feedback received on ED 223.
- AusBC20 When issuing AASB 17 the AASB was aware that a superannuation entity acting in the capacity of an insurer would apply the insurance requirements of AASB 1056 and not those of AASB 17 because AASB 1056 effectively overrides AASB 17 for a superannuation entity acting in the capacity of an insurer. The AASB noted this would mean superannuation entities could not claim compliance with IFRS. However, the AASB noted that superannuation entities could not claim IFRS compliance anyway because AASB 1056 does not incorporate the corresponding IASB Standard. Accordingly, the AASB decided that no amendments were necessary to the insurance requirements of AASB 1056 as IFRS compliance is not an objective in this limited circumstance. For the avoidance of doubt, the AASB also decided to prevent superannuation entities from applying AASB 17 through an amendment to AASB 1057 *Application of Australian Accounting Standards*. Consequently, the AASB deleted a cross-reference to IAS 26 from paragraph 7(b) of AASB 17 instead of replacing it with a cross-reference to AASB 1056.
- AusBC21 The AASB also considered groups where the consolidated financial statements of a superannuation entity include an insurance subsidiary that applies AASB 17. On this issue the AASB noted that no significant issues were brought to its attention during the development of either AASB 1056 or AASB 17, nor since.
- AusBC22 Accordingly, the AASB decided to issue AASB 17 without any consequential amendments to the insurance requirements of AASB 1056 in relation to this matter. However, the AASB decided that it would add a specific matter for comment on this matter to its forthcoming ED on Australian-specific issues arising from AASB 17.

Implications for NFP and public sector entities

- AusBC23 When issuing a new accounting Standard the AASB considers the applicability of that Standard to all sectors of the economy. In the case of AASB 17, the incorporation of IFRS 17 means that the for-profit private sector is largely considered through the IASB’s due process – see paragraphs AusBC6–AusBC11.
- AusBC24 However, the IASB does not explicitly consider:
- (a) NFP entities in the public and private sectors; and
 - (b) for-profit entities in the public sector.
- AusBC25 The AASB decided that additional consideration is warranted for such entities. To that end, the AASB established a short-term project to consider the applicability and suitability of AASB 17 to them.
- AusBC26 At the time of issuing AASB 17, that project was in the process of developing proposals for exposure in the AASB’s forthcoming ED on Australian-specific issues arising from AASB 17.
- AusBC27 Notwithstanding the above project, the AASB was aware of key concerns from the NFP public sector in particular that need further consideration before a decision is made about whether those entities should be subject to AASB 17 without amendment. Chiefly among those concerns was AASB 17 applicability

to statutory obligations such as Medicare, the National Disability Insurance Scheme or worker's compensation insurance.

- AusBC28 The AASB acknowledged those concerns and decided to temporarily exclude NFP public sector entities from the scope of AASB 17 pending the outcome of its separate project to address these issues. Until such time as the NFP public sector issues are addressed, those affected entities continue to be subject to AASB 4, AASB 1023 and AASB 1038 (and, potentially, Interpretation 1047).
- AusBC29 The AASB noted that NFP private sector entities (eg some health insurers) often enter into insurance contracts that are substantively similar to those entered into by for-profit entities. Accordingly, the AASB decided not to restrict NFP private sector entities from applying AASB 17, rather allowing those entities to decide to apply AASB 17 prior to 1 January 2021. However, the AASB may propose additional application guidance, where necessary, as part of the forthcoming ED on Australian-specific issues arising from AASB 17, the aim of which is to be operative before the mandatory application date of AASB 17.
- AusBC30 The AASB also noted that for-profit public sector entities could enter into arrangements that exhibit characteristics of insurance contracts but are entered into through legislative means as opposed to contractual means. These types of arrangements will also be considered in the AASB's forthcoming ED on Australian-specific issues. However, for-profit public sector entities are not prohibited from applying AASB 17 as their not-for-profit counterparts are.

Implications for RDR

- AusBC31 At the time of issuing AASB 17, the AASB was in the process of reviewing its Tier 2 decision-making framework and RDR for existing Standards through ED 277 *Reduced Disclosure Requirements for Tier 2 Entities* (issued in January 2017). Accordingly, the AASB decided not to consider any new pronouncements for RDR concessions until that review is finalised. Consistent with this decision, AASB 17 and its consequential amendments do not include any RDR concessions.
- AusBC32 Once the AASB has finalised its Tier 2 decision-making framework it will make RDR proposals, where appropriate, for AASB 17 and its consequential amendments.